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Legislative Audit Division

State of Montana

Report to the Legislature

April 2006

Financial Audit

For the Fiscal Year Ended June 30, 2005

Montana Water Pollution Control and Drinking Water State Revolving Fund Programs

Department of Environmental Quality
Department of Natural Resources and Conservation

We performed a financial audit of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs for the fiscal year ended June 30, 2005. This report contains the audited financial statements and accompanying notes for fiscal year 2004-05. We issued an unqualified opinion on the financial statements. This opinion means the reader may rely on the financial information presented.

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FINANCIAL AUDITS

Financial audits are conducted by the Legislative Audit Division to determine if the financial statements included in this report are presented fairly and the agency has complied with laws and regulations having a direct and material effect on the financial statements. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

The Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports in addition to those required by Government Auditing Standards. This individual agency audit report is not intended to comply with these requirements. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2005, was issued March 6, 2006. The Single Audit Report for the two fiscal years ended June 30, 2007, will be issued by March 31, 2008. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
State Capitol
Helena MT 59620
Phone (406) 444-3616

Legislative Audit Division
Room 160, State Capitol
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Helena MT 59620-1705

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Scott A. Seacat, Legislative Auditor
Tori Hunthausen,
Chief Deputy Legislative Auditor

Deputy Legislative Auditors:
James Gillett
Jim Pellegrini

April 2006

The Legislative Audit Committee
of the Montana State Legislature:

This is our report on the fiscal year 2004-05 financial audit of the Montana Water Pollution Control State Revolving Fund (WPCSRF) and Drinking Water State Revolving Fund (DWSRF) Programs. The Department of Natural Resources and Conservation requested the audit of these programs because annual audits are required by the federal Environmental Protection Agency. These programs are administered jointly by the Department of Natural Resources and Conservation and the Department of Environmental Quality.

The objectives of a financial audit include determining if the programs' financial statements present fairly their financial position at June 30, 2005, and the results of the programs' operations for the fiscal year then ended. We tested compliance with state and federal laws that have a direct and material impact on the financial statements.

The WPCSRF program provides loans at a reduced interest rate to finance construction of publicly owned water pollution control facilities, nonpoint source pollution control projects, and estuary management plans. Water pollution control loans are comprised of federal grants and state match funds, and must be repaid within 30 years. As of June 30, 2005, the WPCSRF had $135,777,154 of outstanding loans, including advances from other funds.

The DWSRF program provides low interest loans to communities for the construction of drinking water treatment facilities. Drinking water loans are comprised of federal grants and state match funds, and may be financed up to 30 years. At June 30, 2005, the DWSRF had $52,140,592 of outstanding loans.

On page A-1, you will find the Independent Auditor's Report followed by the financial statements and accompanying notes. We issued an unqualified opinion which means the reader can rely on the presented information. The programs' financial statements begin on page A-3. Our opinion on the programs' supplementary financial information is on page B-1. The supplementary information begins on page B-3. Beginning on page C-1 is our report on compliance and internal control, which is required by Government Auditing Standards issued by the Comptroller General of the United States.

Officials from both departments have reviewed this report and agree with the contents. The Department of Environmental Quality's response is at page D-1. We thank the directors of the Department of Environmental Quality and the Department of Natural Resources and Conservation and their staff for their cooperation and assistance during the audit

Respectfully submitted,

Scott A. Seacat
Legislative Auditor

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Appointed and Administrative Officials

Department of Environmental Quality	Richard Opper, Director
	Tom Livers, Deputy Director
	Dean Rude, Chief Financial Officer, Financial Services
Department of Natural Resources and Conservation	Mary Sexton, Director
	Anna Miller, Financial Advisor
	Ann Bauchman, Administrator, Centralized Services Division

For additional information concerning the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs, contact Anna Miller, Financial Advisor, at:

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Helena MT 59620-1601
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e-mail: annam@mt.gov

The audit staff involved in this audit were Alexa O'Dell, Rick Eneas, Cindy Jorgenson, Jim Manning and Jeff Tamblyn.

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
Tori Hunthausen,
Chief Deputy Legislative Auditor

Deputy Legislative Auditors:
James Gillett
Jim Pellegrini

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Combined Balance Sheet of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs as of June 30, 2005, and the related Combined Statement of Revenues, Expenditures, and Changes in Fund Balances for the fiscal year then ended. The information contained in these financial statements is the responsibility of the management of the Montana Department of Environmental Quality and the Montana Department of Natural Resources and Conservation. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

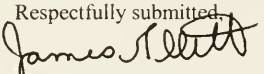
As discussed in the notes to the financial statements, the financial statements of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs are intended to present the financial position and results of operations of only that portion of the financial reporting entity of the state of Montana that is attributable to the transactions of the programs.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs as of June 30, 2005, and results of operations for the fiscal year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards,* we have also issued our report dated February 10, 2006, on our consideration of the programs' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters.

The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Respectfully submitted,



James Gillett, CPA
Deputy Legislative Auditor

February 10, 2006

MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
STATE REVOLVING FUND PROGRAMS
COMBINED BALANCE SHEET
SPECIAL REVENUE AND DEBT SERVICE FUNDS
JUNE 30, 2005

	WATER POLLUTION CONTROL			DRINKING WATER			
ASSETS	STATE SPECIAL REVENUE	FEDERAL SPECIAL REVENUE	DEBT SERVICE	STATE SPECIAL REVENUE	FEDERAL SPECIAL REVENUE	DEBT SERVICE	TOTAL
Cash and Cash Equivalents	$3,545,428	$38,588	$641,594	$2,359,751	$100,153	$464,324	$7,169,838
Interest Receivable	354,795		1,485,857	82,789		344,930	2,268,451
Due from Federal Government					63,715		63,715
Investments	4,364,444		2,638,641	9,241,731		1,315,511	17,558,327
Loans Receivable	123,406,127			52,140,592			175,546,719
Advances to Other Funds	12,371,027						12,371,027
Total Assets	$144,041,821	$38,588	$4,764,192	$63,824,843	$163,868	$2,144,765	$214,978,077
LIABILITIES AND FUND BALANCES							
Liabilities							
Accounts Payable	$14,889	$11		$10,715	$61,632		$87,247
Payroll Payable	1,574	5,645			35,900		43,319
Interest Payable	34,340			190,540	178		225,058
Deferred Revenue		35,180			66,158		101,338
Total Liabilities	$50,803	$41,036		$201,255	$163,868		$456,962
Fund Balances							
Reserved for Loans Receivable	$123,406,127			$52,140,592			$175,546,719
Reserved for Debt Service			4,764,192			2,146,278	6,910,470
Unreserved, Undesignated	20,584,891	(2,448)		11,482,996		(1,513)	32,063,926
Total Fund Balances	$143,991,018	($2,448)	$4,764,192	$63,623,588		$2,144,765	$214,521,115
Total Liabilities and Fund Balances	$144,041,821	$38,588	$4,764,192	$63,824,843	$163,868	$2,144,765	$214,978,077

The accompanying notes to the financial statements are an integral part of this statement.

MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
STATE REVOLVING FUND PROGRAMS
COMBINED STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
SPECIAL REVENUE AND DEBT SERVICE FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	WATER POLLUTION CONTROL			DRINKING WATER			
	STATE SPECIAL REVENUE	FEDERAL SPECIAL REVENUE	DEBT SERVICE	STATE SPECIAL REVENUE	FEDERAL SPECIAL REVENUE	DEBT SERVICE	TOTAL
REVENUES:							
Federal Capitalization Grant Revenue		$2,000,865			$4,651,120		$6,651,985
Interest Income on Investments	$362,295		($1,049)	$155,585		$216,394	753,225
Other Investment Income	45,186		17,645	(302,562)		(29,381)	(268,910)
Interest Income from Loans	1,004,655		4,165,817	362,542		1,539,904	7,073,118
Other Income	7	37			105		149
TOTAL REVENUES	$1,432,345	$2,000,902	$4,182,813	$215,585	$4,651,225	$1,726,917	$14,209,567
EXPENDITURES:							
Program Administration/Set-Asides	$83,300	$369,383		$59,447	$1,211,171		$1,723,301
TOTAL EXPENDITURES	$83,300	$369,383		$59,447	$1,211,171		$1,723,301
Excess Revenues Over (Under) Expenditures	$1,349,045	$1,631,519	$4,182,813	$156,118	$3,440,054	$1,726,917	$12,486,266
OTHER FINANCING SOURCES:							
General Obligation Bonds Face Amount	$2,110,000			$3,675,000			$5,985,000
General Obligation Bond Premium	61,502			138,476			199,978
Operating Transfers In							
Recycled Transfers from Drinking Water WRF	3,655,403						3,655,403
Recycled Transfer from Water Pollution Control SRF				85,000			85,000
Debt Service Sweep				395,754			395,754
Transfer from Debt Service to Principal for Loans				43,400			43,400
Bond Anticipation Note (BAN) Proceeds	500,000						500,000
Bond Proceeds to Debt Service for BAN pay-off			500,000				500,000
Loan Loss Reserve Sweep	1,194,699			421,554			1,616,253
Transfer from Investment Fund for Bond Payments			693,086				693,086
Federal Capitalization Grants	1,629,173			3,458,597			5,087,770
Total Other Financing Sources	$9,150,777		$1,393,086	$8,417,781			$18,961,644
OTHER FINANCING USES:							
Bond Principal			$2,225,000			$435,000	$2,660,000
Bond Interest			705,974			433,092	1,139,066
Bonds Cost of Issuance	$67,176			$94,936			162,114
Operating Transfers Out							
Recycled Transfer to Water Pollution Control SRF				3,655,403			3,655,403
Recycled Transfer to Drinking Water WRF	85,000						85,000
Debt Service Sweep						395,754	395,754
Transfer from Debt Service to Principal for Loans						43,400	43,400
Transfer BAN Liability to Debt Service			500,000				500,000
Bond Proceeds to Debt Service for BAN pay-off	500,000						500,000
Loan Loss Reserve Sweep			1,194,699			421,554	1,616,253
Transfer to Debt Service for Bond Payments	693,086						693,086
Federal Capitalization Grants		1,629,037			3,458,597		5,087,634
Total Other Financing Uses	$1,545,264	$1,629,037	$4,825,873	$3,750,339	$3,458,597	$1,728,800	$16,737,710
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	$8,954,558	$2,462	$950,026	$4,623,560	($16,543)	($1,883)	$14,710,200
Fund Balances, July 1, 2004	$135,684,121	($39,746)	$3,779,439	$58,817,358	$61,571	$2,146,160	$200,450,903
Prior Year and Federal Revenue Adjustments	(647,661)	34,816	34,726	(17,330)	(43,026)	(1,512)	(639,987)
Fund Balances, June 30, 2005	$143,991,016	($2,448)	$4,764,192	$63,623,586	$0	$2,144,765	$214,521,116

The accompanying notes to the financial statements are an integral part of this statement.

MONTANA STATE WATER POLLUTION CONTROL AND DRINKING WATER STATE REVOLVING FUND PROGRAMS SPECIAL REVENUE AND DEBT SERVICE FUND NOTES TO FINANCIAL STATEMENTS FOR THE FISCAL YEAR ENDED JUNE 30, 2005

1. Organization of the Programs

The State of Montana Water Pollution Control State Revolving Fund (WPCSRF) Program was established pursuant to Title VI of the Federal Water Quality Act of 1987. This federal act established the WPCSRF program to replace the construction grants program to provide a flexible financing source to loan money at reduced interest rates to finance the construction of publicly owned water pollution control facilities, non-point source pollution control projects, and estuary management plans. Instead of making grants to communities that pay for a portion of building wastewater treatment facilities, the WPCSRF provides for low interest rate loans to finance the entire cost of qualified projects.

The State of Montana Drinking Water State Revolving Fund (DWSRF) Program was established pursuant to Title XIV of the Safe Drinking Water Act. This federal act established the DWSRF program for states to make loans to community water systems and non-profit non-community water systems. Instead of making grants to communities that pay for a portion of building drinking water treatment facilities, the DWSRF provides for low interest rate loans to finance the entire cost of qualified projects or to refinance debt obligations on projects that began after July 1, 1993. The State of Montana first incurred expenditures in the DWSRF Program in state fiscal year (SFY) 1997.

WPCSRF loans must be repaid within 30 years while DWSRF loan agreements allow up to 30 years for repayment. All repayments of interest and principal must remain in the revolving funds. Both programs are capitalized through U.S. Environmental Protection Agency (EPA) grants. States are required to provide 20 percent of the federal capitalization grant as matching funds in order to receive a grant. The State of Montana issues General Obligation Bonds to provide the required state matching funds.

The programs are jointly administered by the Technical and Financial Assistance Bureau of the Department of Environmental Quality (DEQ) and the Conservation and Resource Development Division of the Department of Natural Resources and Conservation (DNRC). The revolving fund programs do not have any full time employees. Both funds are charged for time spent on SRF activities by department employees. The charges include salaries and benefits of the employees and operating expenses as well as indirect costs.

2. Summary of Significant Accounting Policies

A. State Revolving Fund (SRF) Program Fund Structure

Both programs use Special Revenue and Debt Service funds, as appropriate, to report the financial position and the results of operations. A Special Revenue Fund accounts for the

proceeds of specific revenue sources that are restricted to expenditures for specified purposes (other than expendable trusts or major capital projects). A Debt Service Fund accounts for resources accumulated for payment of principal and interest on general long-term obligation debt. Montana maintains a State Special Revenue and a Federal Special Revenue Fund. The SRF program revenue and expenses include transactions from each Special Revenue Fund. Special Revenue and Debt Service Funds are considered governmental funds.

A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions and activities.

B. Basis of Accounting

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for using a current financial resources measurement focus. Current financial resources means that, generally, only assets and current liabilities are included on the balance sheet. Operating statements of governmental funds present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets.

Governmental funds use the modified accrual basis of accounting. The modified accrual basis is the accrual basis adapted to the governmental fund-type measurement focus. Under the modified accrual basis of accounting, revenues are recorded when received in cash unless susceptible to accrual. Revenues are susceptible to accrual if they are measurable and available within sixty days after the end of the fiscal year to finance expenditures of the fiscal year. Revenues are deferred if material and received before the normal time of receipt or if received for a particular activity and the expense for that activity has not been incurred prior to fiscal year-end. Expenditures are recognized when the related fund liability is incurred, with the following exceptions:

1) principal and interest on long-term debt are recognized when due;
2) prepayments are accounted for as expenditures in the period of acquisition;
3) inventory items are considered expenditures when purchased.

The Loans Receivable account resides in the State Special Revenue fund for each program. This account represents the total principal due on the loans outstanding for each program.

C. Prior Period Adjustments

Prior period adjustments reported in the accompanying financial statements relate to corrections of errors from prior periods. The most significant of these adjustments affected the Water Pollution Control State Special Revenue column in the Combined Balance Sheet and the WPC-SRF Special Revenue columns in the Schedule of Revolving and Non-Revolving SRF Program Assets. The adjustments relate to corrections to cash with trustee balances that are adjusted as of fiscal year end to reclassify invested cash.

3. Cash/Cash Equivalents

Cash and cash equivalents consist of funds deposited with the US Bank, N.A. as trustee, and include investments categorized as cash equivalents. Cash equivalents are defined as short-term, highly liquid investments with original maturities of three months or less.

Disclosures Relating to Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. In accordance with the investment policy defined in the bonds trust indenture, the cash equivalent funds invested by US Bank, N.A., as trustee, are held in a Treasury Obligations Money Market Fund that invests exclusively in short-term U.S. Treasury obligations and repurchase agreements secured by U.S. Treasury obligations. The U.S. Treasury obligations in which the fund invests include U.S. Treasury bonds, notes, and bills, and are backed by the full faith and credit of the United States government.

Disclosures Relating to Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party.

The investment policy as defined in the Indenture of Trust, and contract with the trustee, does not require collateralization for cash and securities held by the trustee. Securities are registered with the Federal Reserve Bank under "U.S. Bank as trustee for the State of Montana Department of Natural Resources and Conservation." However, U.S. Bank policy is to collateralize money market funds at 101% of cost.

Disclosures Relating to Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The investment policy for the programs, as specified in the Indenture of Trust, does not explicitly address interest rate risk. However, the investment policy implicitly limits interest rate risk for cash equivalents by emphasizing liquidity, holding investments to maturity, and narrowly defining the eligible investments. In general, a shorter average maturity for fixed-income securities held in the money market fund means less sensitivity to interest rate changes. The average maturity in the fund as of December 31, 2005 is nine days. An effective duration method result of NA indicates that interest rate risk is not applicable.

Investment Type	Book Value	Moody's Rating	Effective Duration
Held by trustee:			
Money market funds	$6,907,460	AAA	NA

4. Investments

Power to Invest and Investment Policy

The Board of Examiners of the State of Montana authorizes the sale of general obligation bonds to provide the state match for the SRF programs through the issuance of an Indenture of Trust. The Board of Examiners is comprised of the Governor, Attorney General and the Secretary of State for the State of Montana. The Indenture of Trust specifies the eligible investments meeting defined rating and risk criteria in which the state may invest. The state invests funds through its trustee bank, US Bank, N.A.

Eligible investments are limited, generally, to obligations of, or guaranteed as to principal and interest by, the United States of America, or by any agency or instrumentality thereof. A primary investment objective is to make investments that mature, or are subject to redemption, on or prior to the date or dates that the department anticipates that money will be required to make payments.

Disclosures Relating to Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The short- and long-term investments made by US Bank, N.A., as trustee, are held in U.S. Treasury bills and notes. U.S. Treasury bills have maturities of one year or less and U.S. Treasury notes have maturities greater than one year from the date of issuance.

Disclosures Relating to Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party.

The investment policy as defined in the Indenture of Trust, and contract with the trustee, does not require collateralization for cash and securities held by the trustee. Securities are registered with the Federal Reserve Bank under "U.S. Bank as trustee for the State of Montana Department of Natural Resources and Conservation."

Disclosures Relating to Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The investment policy, as specified in the Indenture of Trust, does not explicitly address interest rate risk. However, the investment policy implicitly limits interest rate risk by emphasizing liquidity, holding investments to maturity, and narrowly defining the eligible investments. The following table includes the Effective Duration calculation for appropriate investment types, or NA to indicate that interest rate risk is not applicable. All funds of the State of Montana are required to use the effective duration method to calculate and report interest rate risk. A lower effective duration number means that there is a lower interest rate risk.

Investment Type	Book Value	Effective Duration
Held by trustee:		
U.S. Treasury bills	$ 2,167,192	NA
U.S. Treasury notes	$15,952,284	2.06

5. Loans Receivable

Montana operates both SRF programs as direct loan programs. Loans made to communities through the Water Pollution Control Program are funded 83.33 percent by the federal EPA capitalization grant, and 16.67 percent by the state match amount. Some Water Pollution Control Program loans are made as recycled, or "second round", loans and are disbursed from loan repayment funds. Loans made by the Drinking Water Program are funded approximately 80 percent by the federal EPA capitalization grant, and 20 percent by the state match amount. The Drinking Water Program makes recycled loans that are disbursed from loan repayment funds. Loan funds are disbursed to the local borrower agencies by the trustee bank as the local borrower agencies expend funds for the purposes of the loan and request reimbursement from the program. Interest is calculated from the date that funds are disbursed. Typically after the final disbursement has been made, the payment schedule is certified in the loan agreement and adjusted for the actual amounts disbursed. No provision for uncollectible accounts has been made as all loans are current in terms of compliance with the repayment schedules, and management believes that all loans will be repaid according to the terms of the loan agreements.

The drawn and outstanding principal balance of all loans guaranteed by the WPCSRF Program as of June 30, 2005 is $135,777,154. The total loans receivable in the WPCSRF program includes $123,406,127 presented as loans receivable and $12,371,027 presented as advances to other funds. The advances are inter-fund loans within the Department of Natural Resources and Conservation used for the non-point source private loans program. The drawn and outstanding principal balance of all loans guaranteed by the DWSRF Program as of June 30, 2005 is $52,140,592.

Loans mature at various intervals through July 1, 2031. The scheduled principal payments on loans and advances to other funds maturing in the years following state fiscal year (SFY) 2005 are as follows:

SFY ending June 30:	WPCSRF Amount	DWSRF Amount
2006	$ 6,183,133	$ 1,702,496
2007	7,656,200	2,906,500
2008	7,602,900	3,128,600
2009	7,899,000	3,141,604
2010 and thereafter	106,435,921	41,261,392
Total	**$ 135,777,154**	**$ 52,140,592**

As of June 30, 2005, the WPCSRF and DWSRF had authorized loans to public entities of the State of Montana that in the aggregate exceeded $188 and $64 million, respectively. The outstanding balances of the largest loans in each portfolio are as follows:

Water Pollution Control State Revolving Fund:

Local Agency	Authorized Loan Amount	Outstanding Balance
City of Great Falls	$ 11,295,267	$ 9,820,000
City of Helena	9,320,000	8,791,000
Big Sky County Water & Sewer	7,000,000	6,645,000
Big Sky County Water & Sewer	6,500,000	5,032,711
Big Sky County Water & Sewer	5,513,000	3,146,000
City of Lewistown	5,400,000	5,084,714
Missoula WWTP	5,000,000	4,569,000
City of Missoula SID 524	4,577,000	4,484,000
Missoula County Mullan Rd RSID 8474	4,498,121	4,418,000
City of Great Falls	4,400,000	4,161,491
Total	**$ 63,503,388**	**$ 56,151,916**

Drinking Water State Revolving Fund:

Local Agency	Authorized Loan Amount	Outstanding Balance
City of Havre II	$ 8,401,000	$ 8,003,000
City of Whitefish II	5,839,000	4,540,000
City of Laurel	5,250,000	3,862,000
City of East Helena II	3,234,000	2,825,000
City of Great Falls	3,000,000	2,514,000
Laurel II	2,541,000	2,320,000
River Rock Water & Sewer	2,100,000	1,949,000
Big Sky County Water & Sewer	1,966,000	1,933,000
City of Conrad II	1,543,172	1,354,000
Fort Peck Rural County WD	1,520,000	1,319,410
Total	**$ 35,394,172**	**$ 30,619,410**

6. Interest Receivable

The interest receivable represents interest owed by borrowers as of June 30, 2005, for the July 1, 2005 payment. It represents the six months of interest accrued from the previous loan payment date of January 1, 2005. Interest receivable balances include $354,795 in the WPCSRF Special Administration fund and $1,485,957 in the WPCSRF Debt Service and Loan Loss Reserve funds, and $82,769 in the DWSRF Special Administration fund and $344,930 in the DWSRF Debt Service and Loan Loss Reserve funds. Interest receivable does not include interest payments received in June, 2005 that were due July 1, 2005. Interest payments received during June, 2005 amounted to $804,013 for the WPCSRF and $730,028 for the DWSRF.

7. Bonds Payable

Water Pollution Control SRF general obligation bonds payable at June 30, 2005 were as follows:

Series 1996C

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2006	3.75 – 5.75	$ 140,000	$ 101,620	$ 241,620
2007		145,000	94,280	239,280
2008		155,000	86,403	241,403
2009		160,000	77,975	237,975
2010		170,000	68,980	238,980
2011-2015		900,000	188,829	1,088,829
2016-2017		235,000	13,656	248,656
Total Cash Requirements		$1,905,000	$ 631,743	$ 2,536,743

Series 1998A

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2006	3.75 – 5.15	$ 145,000	$ 129,635	$ 274,635
2007		150,000	123,218	273,218
2008		155,000	116,469	271,469
2009		165,000	109,308	274,308
2010		170,000	101,685	271,685
2011-2015		985,000	374,401	1,359,401
2016-2019		975,000	102,781	1,077,781
Total Cash Requirements		$2,745,000	$ 1,057,497	$ 3,802,497

Series 2000B

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2006	4.25 – 5.60	$ 120,000	$ 149,570	$ 269,570
2007		125,000	143,659	268,659
2008		130,000	137,459	267,459
2009		135,000	130,983	265,983
2010		145,000	124,086	269,086
2011-2015		855,000	498,138	1,353,138
2016-2020		1,125,000	237,254	1,362,254
2021		270,000	7,560	277,560
Total Cash Requirements		$2,905,000	$ 1,428,709	$ 4,333,709

Series 2001H

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2006	4.00 – 5.00	$ 100,000	$ 107,195	$ 207,195
2007		105,000	103,095	208,095
2008		110,000	98,795	208,795
2009		115,000	94,295	209,295
2010		115,000	89,695	204,695
2011-2015		660,000	369,706	1,029,706
2016-2020		820,000	200,176	1,020,176
2021-2022		390,000	19,750	409,750
Total Cash Requirements		$2,415,000	$ 1,082,707	$ 3,497,707

Series 2003D

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2006	2.00 – 3.75	$ 155,000	$ 76,150	$ 231,150
2007		160,000	73,000	233,000
2008		160,000	69,800	229,800
2009		165,000	66,426	231,426
2010		170,000	62,613	232,613
2011-2015		925,000	236,964	1,161,964
2016-2019		850,000	65,250	915,250
Total Cash Requirements		$2,585,000	$ 650,203	$ 3,235,203

Series 2004A

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2006	2.00 – 4.50	$ 125,000	$ 92,948	$ 217,948
2007		150,000	90,198	240,198
2008		150,000	87,198	237,198
2009		155,000	83,760	238,760
2010		160,000	79,623	239,623
2011-2015		870,000	317,521	1,187,521
2016-2020		1,055,000	122,738	1,177,738
Total Cash Requirements		$2,665,000	$ 873,986	$ 3,538,986

Series 2005G

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2006	4.00 – 4.75	$ 0	$ 62,701	$ 62,701
2007		90,000	88,490	178,490
2008		110,000	84,490	194,490
2009		115,000	79,990	194,990
2010		120,000	75,290	195,290
2011-2015		665,000	300,188	965,188
2016-2020		820,000	136,194	956,194
2021		190,000	3,990	193,990
Total Cash Requirements		$2,110,000	$ 831,333	$ 2,941,333

TOTAL GENERAL OBLIGATION DEBT - WPCSRF

Payable during the year ending June 30,	Principal	Interest	Total
2006	$ 785,000	$ 719,819	$ 1,504,819
2007	925,000	715,940	1,640,940
2008	970,000	680,614	1,650,614
2009	1,010,000	642,737	1,652,737
2010	1,050,000	601,972	1,651,972
2011-2015	5,860,000	2,285,747	8,145,747
2016-2020	5,880,000	878,049	6,758,049
2021-2022	850,000	31,300	881,300
Total Cash Requirements	$17,330,000	$ 6,556,178	$ 23,886,178

Drinking Water SRF general obligation bonds payable at June 30, 2005 were as follows:

Series 1998F

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2006	3.60 – 4.85	$ 130,000	$ 108,182	$ 238,182
2007		140,000	102,747	242,747
2008		145,000	96,940	241,940
2009		150,000	90,855	240,855
2010		155,000	84,449	239,449
2011-2015		885,000	310,773	1,195,773
2016-2019		860,000	85,105	945,105
Total Cash Requirements		$2,465,000	$ 879,051	$ 3,344,051

Series 2000A

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2006	4.25 – 5.60	$ 105,000	$ 134,180	$ 239,180
2007		110,000	128,993	238,993
2008		120,000	123,401	243,401
2009		125,000	117,413	242,413
2010		130,000	111,133	241,133
2011-2015		765,000	446,418	1,211,418
2016-2020		1,010,000	212,235	1,222,235
2021		240,000	6,720	246,720
Total Cash Requirements		$2,605,000	$ 1,280,493	$ 3,885,493

Series 2001G

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2006	4.00 – 5.00	$ 120,000	$ 127,365	$ 247,365
2007		125,000	122,465	247,465
2008		125,000	117,465	242,465
2009		135,000	112,265	247,265
2010		140,000	106,765	246,765
2011-2015		785,000	439,316	1,224,316
2016-2020		980,000	237,730	1,217,730
2021-2022		460,000	23,250	483,250
Total Cash Requirements		$2,870,000	$ 1,286,621	$ 4,156,621

Series 2003E

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2006	2.15 – 3.75	$ 95,000	$ 46,785	$ 141,785
2007		95,000	44,885	139,885
2008		100,000	42,935	142,935
2009		100,000	40,860	140,860
2010		105,000	38,525	143,525
2011-2015		560,000	146,555	706,555
2016-2019		530,000	40,688	570,688
Total Cash Requirements		$1,585,000	$ 401,233	$ 1,986,233

Series 2005F

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2006	4.00 – 4.75	$ 0	$ 116,458	$ 116,458
2007		160,000	164,500	324,500
2008		200,000	157,300	357,300
2009		210,000	149,100	359,100
2010		215,000	140,600	355,600
2011-2015		1,225,000	562,338	1,787,338
2016-2020		1,515,000	259,475	1,774,475
2021		350,000	7,350	357,350
Total Cash Requirements		$3,875,000	$ 1,557,121	$ 5,432,121

TOTAL GENERAL OBLIGATION DEBT - DWSRF

Payable during the year ending June 30,	Principal	Interest	Total
2006	$ 450,000	$ 532,970	$ 982,970
2007	630,000	563,590	1,193,590
2008	690,000	538,041	1,128,041
2009	720,000	510,493	1,230,493
2010	745,000	481,472	1,226,472
2011-2015	4,220,000	1,905,400	6,125,400
2016-2020	4,895,000	835,233	5,730,233
2021-2022	1,050,000	37,320	1,087,320
Total Cash Requirements	$13,400,000	$ 5,404,519	$ 18,804,519

8. Fund Balance

A portion, or all, of the fund balances in the WPCSRF and DWSRF have been reserved for Loans Receivable and Debt Service, indicating that a portion, or all, of the fund balances are not available for current expenditures.

9. Program Capitalization

The WPCSRF and DWSRF programs are capitalized by grants from the Environmental Protection Agency (EPA) and matching funds from the State of Montana. All grant funds drawn are recorded as revenue. As of June 30, 2005, the EPA has awarded capitalization grants of $114,160,565 to the State of Montana for the WPCSRF program; $188,174,656 has been drawn from federal and state funds for loans and administrative expenses. As of June 30, 2005, the EPA has awarded capitalization grants of $77,602,488 to the State of Montana for the DWSRF program; $65,653,619 has been drawn from federal and state funds for loans and administrative expenses. Montana has issued general obligation bonds totaling $24,590,000 for use as state matching funds for the WPCSRF program and $14,795,000 for use as state matching funds in the DWSRF program.

10. Federal Capitalization Grant Revenues

Actual draws of federal funds differ from the amount of Federal Capitalization Grant Revenue reported on the Statement of Revenues, Expenditures and Changes in Fund Balance. This occurs because state accounting policy requires federal special revenue funds reflect a zero fund balance at fiscal year-end (with the exception of "A" accruals). Consequently, if a positive fund balance exists, deferred revenue is recorded. If a negative fund balance is reflected at fiscal year-end, a revenue accrual to record revenue is recorded to zero the fund balance.

The following is a reconciliation of federal revenues reported on the financial statements to federal cash actually drawn during the state fiscal year:

	WPCSRF
Federal Capital Grant Revenue – Combined Statement	$ 2,000,865
Adjustment Due from Federal Govt. FY04	19,402
Adjustment Deferred Revenue FY04	(59)
Adjustment Due from Federal Govt. FY05	0
Adjustment Deferred Revenue FY05	(35,180)
Other Adjustments	(37)
Total Federal Draws	**$ 1,984,991**

	DWSRF
Federal Capital Grant Revenue – Combined Statement	$ 4,657,374
Adjustment Due From Federal Govt. FY04	168,855
Adjustment Deferred Revenue FY04	(19,382)
Adjustment Due From Federal Govt. FY05	63,716
Adjustment Deferred Revenue FY05	(66,158)
Other Adjustments	(105)
Total Federal Draws	**$ 4,804,300**

11. Interest Income on Investments

This revenue represents interest earnings on investments within the funds. All assets of the funds are fully invested by the trustee, to the degree possible, in investment vehicles. The investments range from U.S. Treasury obligation money market funds to long-term government securities. Interest income earned in one fund but transferred to another fund in accordance with terms of the bond indenture is reported in the receiving fund in which it becomes available for expenditure.

12. Other Investment Income

This revenue represents unamortized (premium) and discount recognized upon maturity or disposal of government securities, as well as the change in unrealized appreciation and (depreciation) in the market value of investments as of June 30, 2005.

13. Interest Income from Loans

This revenue represents interest earnings from loan repayments made by borrowers. A typical loan carries an interest rate of 4%; however, during fiscal year 2004 the rate was decreased to 3.75% for new loans and the lower rate was continued through fiscal year 2005. The 3.75% is comprised of a loan interest rate of 2.00%, as well as a 1.00% Loan Loss Reserve fee and a 0.75% Special Administration fee. The interest income for each of these components totaled $2,923,407, $1,242,410, and $1,004.855, respectively, for the WPCSRF program; and $1,102,156, $437,748, and $362,542, respectively, for the DWSRF program. Disadvantaged communities can receive loans with an interest rate of 2.75% because no Loan Loss Reserve fee is levied.

14. Program Administration and Set-Aside Funds

This expenditure represents costs incurred by DEQ and DNRC to administer the SRF programs. This amount is limited to 4% of each grant award from the EPA. Program Administration appears under the Resource Development/Recreation function in the State of Montana Combined Annual Financial Report (CAFR).

The DWSRF program includes several "sub-programs", called set-asides, which states can elect. A State may use a certain portion of its capitalization grants for the following activities:

- up to 4 percent of its capitalization grants to administer the DWSRF and provide technical assistance to public water systems;
- up to 2 percent of its grants to provide assistance to small public water systems;
- up to 10 percent of its grants for state program management activities, including administration of the State Public Water System Supervision Program, administration of the source water protection program, development and implementation of the capacity development and operator certification programs;
- up to 15 percent of its grants to assist in the development and implementation of local drinking water protection initiatives and other State programs.

In the DWSRF, the 4 percent administrative set-aside must be deposited to a separate fund, and must have separate accounting and disclosure.

DWSRF Program Administration/Set-Asides Detail:	
Administration – EPA grants	$ 357,880
Administration – State funds	59,447
Technical Assistance	86,375
State Program Management	419,803
Local Assistance	269,855
Other Expenses	77,258
Total Administration and Set-Asides	$1,270,618

15. Other Financing Sources and Uses

The Recycled Transfer from the DWSRF to the WPCSRF represents the amount transferred between the two programs to fund water pollution control project loans. At the discretion of the Governor, the state may transfer up to 33 percent of the DWSRF capitalization grant to the WPCSRF or an equal amount from the WPCSRF to the DWSRF. The transferred funds are "recycled" such that they consist of principal repayments from previous loans for drinking water projects.

Loan interest amounts received that exceed the debt service requirements are shown as a Financing Source and Use on the financial statements. The balance remaining in the Debt Service fund is transferred to the Investment fund. Both funds are within the State Revolving Fund. This occurs after payments are made to the bondholders on July 15 of each year. In the Arbitrage Certificate, this activity is termed a Debt Service Sweep.

The Loan Loss Reserve Sweep represents cash in excess of the reserve requirement that is transferred from the Loan Loss Reserve fund to the Principal fund per the bond indenture. The Loan Loss Reserve fund is considered to be outside of the State Revolving Fund.

16. Subsequent Events

A portion of the 2003D (Water Pollution Control) and 2003E (Drinking Water) General Obligation bonds were called and redeemed on November 15, 2005 and January 15, 2006. The redemption amounts were:

Date	2003D	2003E
November 15, 2005	$650,000	$650,000
January 15, 2006	395,000	0

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
Tori Hunthausen,
Chief Deputy Legislative Auditor

Deputy Legislative Auditors:
James Gillett
Jim Pellegrini

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs' (programs) financial statements. The Schedule of Revolving and Non-Revolving SRF Program Assets, Special Revenue and Debt Service Funds, for the programs and the related Schedule of Revolving and Non-Revolving SRF Program Revenues, Expenditures, and Changes in Fund Balances, Special Revenue and Debt Service Funds are presented for the purposes of additional analysis and are not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the programs' financial statements and, in our opinion, are fairly stated in all material respects in relation to the programs' financial statements taken as a whole.

Respectfully submitted,

James Gillett, CPA
Deputy Legislative Auditor

February 10, 2006

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MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
SCHEDULE OF REVOLVING AND NON-REVOLVING SRF PROGRAM ASSETS
SPECIAL REVENUE AND DEBT SERVICE FUNDS
REGULATORY BASIS [1]
JUNE 30, 2005

	WPC-SRF SPECIAL REVENUE		WPC-SRF DEBT SERVICE FUND		Drinking Water SPECIAL REVENUE		Drinking Water DEBT SERVICE FUND		
	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	TOTAL
ASSETS									
Cash and Cash Equivalents	$2,839,141	$744,876	$447,828	$193,766	$2,307,684	$152,220	$360,335	$123,988	7,169,838
Interest Receivable		354,795	1,025,698	460,259		82,769	245,362	99,568	2,268,451
Due From Federal Government					63,715				63,715
Investments	2,028,239	2,336,205	1,097,488	1,539,153	7,467,551	1,774,180	480,970	834,541	17,558,327
Loans Receivable	123,406,127				52,140,592				175,546,719
Advances to Other Funds	12,371,027								12,371,027
Total Assets	$140,644,534	$3,435,876	$2,571,014	$2,193,178	$61,979,542	$2,009,169	$1,086,667	$1,058,097	$214,978,077
LIABILITIES AND FUND BALANCES									
Liabilities:									
Accounts Payable	$13	$14,887			$61,632	$10,715			$87,247
Payroll Payable	7,017	402			35,900				43,319
Interest Payable	34,340				190,718				225,058
Deferred Revenue	35,180				66,158				101,338
Total Liabilities	$76,550	$15,289			$354,408	$10,715			$456,962
Fund Balances									
Reserved for Loans Receivable	$123,406,127				$52,140,592				175,546,719
Reserved for Debt Service			$2,571,014	$2,193,178			1,088,181	1,058,097	6,910,470
Unreserved, Undesignated	17,161,858	$3,420,586			9,484,542	1,998,454	(1,514)		32,063,926
Total Fund Balances	$140,567,985	$3,420,586	$2,571,014	$2,193,178	$61,625,134	$1,998,454	$1,086,667	$1,058,097	$214,521,115
Total Liabilities and Fund Balances	$140,644,535	$3,435,876	$2,571,014	$2,193,178	$61,979,542	$2,009,169	$1,086,667	$1,058,097	$214,978,077

[1] This schedule is prepared on a regulatory basis of presentation, rather than a GAAP [2] basis, as requested by the Environmental Protection Agency (EPA) for the Water Pollution Control and Drinking Water State Revolving Fund (SRF) Programs. This presentation separates certain regulated Revolving Fund (within the Fund) and Non-Revolving Fund (outside the Fund) activity by fund type. All proceeds from the EPA Capitalization Grant, corresponding state matching funds, and loan principal and interest repayments must be deposited into the Revolving Fund under Title VI of the Clean Water Act and Title XIV of the Safe Drinking Water Act. Other proceeds, including Administration and Origination Fees and Loan Loss Reserves are deposited into the Non-Revolving Fund and may be used for other water quality purposes under the federal acts mentioned above.

[2] Generally Accepted Accounting Principles (GAAP).

MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
SCHEDULE OF REVOLVING AND NON-REVOLVING SRF PROGRAM
REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
SPECIAL REVENUE AND DEBT SERVICE FUNDS
REGULATORY BASIS [1]
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	WPC-SRF SPECIAL REVENUE		WPC-SRF DEBT SERVICE FUND		Drinking Water SPECIAL REVENUE		Drinking Water DEBT SERVICE FUND		
	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	TOTAL
REVENUES:									
Federal Capitalization Grant Revenue	$2,000,865				$4,651,120				$6,651,985
Interest Income on Investments	208,384	$173,911	$13,086	($14,135)	74,161	$81,424	$216,647	($253)	753,225
Other Investment Income	(87,043)	132,231	6,814	11,032	(250,023)	(52,540)	3,000	(32,381)	(268,910)
Interest Income from Loans	(45)	1,004,900	2,923,407	1,242,410		362,542	1,102,156	437,748	7,073,118
Other Income	44				105				149
Total Revenues	$2,122,205	$1,311,042	$2,943,307	$1,239,307	$4,475,363	$391,426	$1,321,803	$405,114	$14,209,567
EXPENDITURES:									
Program Administration/Set-Asides	$443,507	$9,176			$1,211,171	$59,447			$1,723,301
Total Expenditures	$443,507	$9,176			$1,211,171	$59,447			$1,723,301
Excess Revenues Over (Under) Expenditures	$1,678,698	$1,301,866	$2,943,307	$1,239,307	$3,264,192	$331,979	$1,321,803	$405,114	$12,486,266
OTHER FINANCING SOURCES:									
General Obligation Bonds Face Amount	$2,110,000				$3,875,000				$5,985,000
General Obligation Bond Premium	61,502				138,476				199,978
Operating Transfers In									
Recycled Transfer from Drinking Water WRF	3,655,403								3,655,403
Recycled Transfer from Water Pollution Control SRF					85,000				85,000
Reimburse Proceeds from Program Transfer Fund	15,134								15,134
Transfers for Bonds Cost of Issuance / Refunds	324	$67,178				94,936			162,438
Residual Transfer Costs of Issuance to Proceeds	14,002								14,002
Debt Service Sweep					395,754				395,754
Transfers from Debt Service for Loans					43,400				43,400
Transfer Bond Anticipation Note (BAN) to Debt Servic	500,000								500,000
Bond Proceeds to Debt Service for BAN pay-off			$500,000						500,000
Special Administration Transfer to Principal	2,950,000								2,950,000
Recycled Funds Transfers for Loans	234,055								234,055
Transfer from Investment Fund for Bond Payments			893,086						893,086
Loan Loss Reserve Sweep	1,194,699				421,554				1,616,253
Total Other Financing Sources	$10,735,119	$67,178	$1,393,086		$4,959,184	$94,936			$17,249,503
OTHER FINANCING USES:									
Bond Principal			$2,225,000				$435,000		$2,660,000
Bond Interest			705,974				433,092		1,139,068
Bonds Cost of Issuance		$67,178				$94,936			162,114
Operating Transfers Out									
Recycled Transfer to Water Pollution Control SRF					$3,655,403				3,655,403
Recycled Transfer to Drinking Water WRF	$85,000								85,000
Transfers for Bonds Cost of Issuance / Refunds	67,178	324			94,936				162,438
Residual Transfer Costs of Issuance to Proceeds		14,002							14,002
Debt Service Sweep							395,754		395,754
Transfers from Debt Service for Loans							43,400		43,400
Transfer Bond Anticipation Note to Debt Service			500,000						500,000
Bond Proceeds to Debt Service for BAN pay-off	500,000								500,000
Special Administration Transfer to Principal		2,950,000							2,950,000
Recycled Funds Transfers for Loans		249,053							249,053
Transfer to Debt Service for Bond Payments	893,086								893,086
Loan Loss Reserve Sweep				1,194,699				421,554	1,616,253
Total Other Financing Uses	$1,545,264	$3,280,557	$3,430,974	$1,194,699	$3,750,339	$94,936	$1,307,246	$421,554	$15,025,569
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	$10,868,553	($1,911,513)	$905,419	$44,608	$4,473,037	$331,979	$14,557	($16,440)	$14,710,200
Fund Balances July 1, 2004	$130,082,738	$5,561,637	$1,641,554	$2,137,865	$57,212,958	$1,665,971	$1,073,625	$1,074,535	$200,450,903
Prior Year and Federal Revenue Adjustments	(383,306)	(229,538)	24,041	10,685	(60,861)	504	(1,515)	2	(639,988)
Fund Balances June 30, 2005	$140,567,985	$3,420,586	$2,571,014	$2,193,178	$61,625,134	$1,998,454	$1,086,667	$1,058,097	$214,521,115

[1] This schedule is prepared on a regulatory basis of presentation, rather than a GAAP [2] basis, as requested by the Environmental Protection Agency (EPA) for the Water Pollution Control and Drinking Water State Revolving Fund (SRF) Programs. This presentation separates certain regulated Revolving Fund (within the Fund) and Non-Revolving Fund (outside the Fund) activity by fund type All proceeds from the EPA Capitalization Grant, corresponding state matching funds, and loan principal and interest repayments must be deposited into the Revolving Fund under Title VI of the Clean Water Act and Title XIV of the Safe Drinking Water Act Other proceeds, including Administration and Origination Fees and Loan Loss Reserves are deposited into the Non-Revolving Fund and may be used for other water quality purposes under the federal acts mentioned above

[2] Generally Accepted Accounting Principles (GAAP)

Scott A. Seacat, Legislative Auditor
Tori Hunthausen,
Chief Deputy Legislative Auditor

Deputy Legislative Auditors:
James Gillett
Jim Pellegrini

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND OTHER MATTERS AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the financial statements of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs as of and for the fiscal year ended June 30, 2005, and have issued our report thereon dated February 10, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

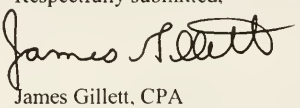
Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Department of Environmental Quality and Department of Natural Resources and Conservation (departments) internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial

statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Legislative Audit Committee, the departments' management, the Montana State Legislature, and the federal Environmental Protection Agency and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Respectfully submitted,



James Gillett, CPA
Deputy Legislative Auditor

February 10, 2006

Montana Department of
ENVIRONMENTAL QUALITY
Brian Schweitzer, Governor
P.O. Box 200901 • Helena, MT 59620-0901 • (406) 444-2544 • www.deq.mt.gov

April 5, 2006

Scott Seacat
Legislative Auditor
Room 160, State Capitol
PO Box 201705
Helena MT 59620-1705

Dear Mr. Seacat:

We have received and reviewed the financial audit of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs for the fiscal year ended June 30, 2005. We are pleased with the unqualified opinion and wish to thank your staff for the professionalism and courtesy with which the audit was conducted.

Sincerely,

for Richard H. Opper, Director

Dean Rude, Chief Financial Officer

APR
LEGISL